

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
Southern Division

FILED

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J.S. [unclear] TO CLERK
N.D. OF ALABAMA

In re:

SHOOK & FLETCHER INSULATION CO.

Debtor-in-Possession.

Cas
Chapter

02-02771

**MOTION FOR AUTHORITY TO PAY
PRE-PETITION WAGES AND BENEFITS TO EMPLOYEES**

Shook & Fletcher Insulation Co., the debtor and debtor-in-possession in this case ("Shook" or the "Debtor"), by counsel, hereby moves the Court for authority to pay pre-petition wages and benefits to its employees (the "Motion"). In support of its Motion, the Debtor respectfully represents:

JURISDICTION AND VENUE

1. This Court has jurisdiction over this Motion pursuant to 28 U.S.C. §§ 157 and 1334(b). This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2). Venue of this proceeding and this Motion is proper in this district pursuant to 28 U.S.C. §§ 1408 and 1409.

2. The statutory basis for the relief sought in this Motion is 11 U.S.C. §§ 105(a), 507(a)(3) and 507(a)(4).

BACKGROUND

3. On April 8, 2002 (the "Petition Date"), Shook filed its voluntary petition under Chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code"). Shook is authorized to operate its business and manage its property as a debtor-in-possession pursuant to Sections 1107(a) and 1108 of the Bankruptcy Code.

12

4. The Debtor incorporates by reference as if fully set forth herein the Declaration of Wayne W. Killion, Jr. in Support of Voluntary Petition and First Day Motions filed with this Court on the Petition Date.

Shook's Current Employee Wages and Benefits

5. As of March 24, 2002, Shook employed 292 personnel, consisting of 28 salaried employees, principally management-level employees (the "Salaried Employees"), 20 employees paid on an hourly basis, principally persons employed in Shook's warehouses (the "Hourly Employees"), and 244 union employees, principally employees who perform installation work pursuant to Shook's installation contracts with its customers (the "Union Employees"). The total number of union employees Shook employs at any given time varies as the volume of its contract work varies. Shook has a loyal and stable workforce, and considers its labor relations, including relations with its workers' unions, very good. As of the Petition Date, Shook had paid all wages and all benefits then due, except for (i) wages and benefit payments reflected in paychecks which had been issued but had not cleared Shook's bank as of the Petition Date, and (ii) wages and benefits due for work performed prior to the Petition Date and for which the routine date of payment had not occurred as of the Petition Date.

Salaried Employee Pay and Benefits

6. Shook's Salaried Employees are compensated twice a month -- each salaried employee may receive an advance at the middle of each month (equal to approximately one-half of his or her monthly salary) and his or her monthly compensation (net of any mid-month advance) at the end of the month. All Salaried Employees utilize Shook's direct-deposit system; as a result, as far as Shook presently is aware, as of the Petition Date there were no checks outstanding for current compensation to Salaried Employees.

7. Because the Petition Date was on April 8, 2002, Salaried Employees worked from April 1, 2002 to the Petition Date, but have not yet been compensated for such pre-petition services.

8. Salaried Employees receive the following benefits (collectively, the “Non-Union Employee Benefits”):

- paid time off of from 5 to 20 days per year (depending upon seniority);
- participation in Shook’s employee medical and dental insurance programs;
- participation in Shook’s 401(k) employee plan;
- participation in Shook’s Group Life Insurance and Long-Term Disability Insurance programs; and
- reimbursement of business expenses, including those incurred in connection with automobile usage, civic dues, and other reimbursable business expenses.

9. With respect to the employee medical and dental insurance programs, Shook pays the premiums associated with the employee’s coverage. Those employees who elect family coverage pay additional premiums, by having fixed amounts withheld from each paycheck.

10. With respect to Shook’s 401(k) employee plan, employees who elect to participate have the agreed amounts withheld from each paycheck.

11. With respect to Group Life Insurance and Long-Term Disability Insurance, Shook provides such insurance coverages to its Salaried Employees at no cost to the employees; that is, Shook pays all costs associated with such programs.

Hourly Employee Wages and Benefits

12. Shook’s Hourly Employees are paid each Wednesday, for services rendered during the week ending the previous Sunday. All Hourly Employees, other than Shook’s Hourly Employees located at its Decatur facility, utilize Shook’s direct-deposit system; as a result, as far

as Shook presently is aware, as of the Petition Date there were no checks outstanding for current wages for such Hourly Employees.

13. Shook's Hourly Employees at its Decatur facility are paid by check drawn upon Shook's Decatur payroll account at SouthTrust Bank (the "Decatur Account"). The Decatur Account is also used to pay Shook's Union Employees (as described below). As of the Petition Date, there were checks outstanding to Hourly Employees at Decatur, who had provided services to Shook pre-petition.

14. Because the Petition Date was on April 8, 2002, Hourly Employees worked from April 1, 2002 to the Petition Date, but have not yet been compensated for such pre-petition services.

15. Hourly Employees receive the same benefits on the same basis as Salaried Employees, except that Hourly Employees do not receive coverage under Shook's Long-Term Disability Plan.

Union Employee Wages and Benefits

16. Shook's Union Employees render services under Shook's contracts to install new insulation or to remove existing insulation. As a result, the total number of Union Employees varies with Shook's contract requirements.

17. Shook currently is a party to certain union agreements¹ (collectively, the "Union Agreements"). By this Motion, Shook does not seek to modify or affect the Union Agreements;

¹ These agreements are:

- Collective Bargaining Agreement with Local 78, International Association of Heat and Frost Insulators & Asbestos Workers (the "Union"), as amended, dated September 24, 2001 (which expires September 26, 2004); and

- Project Agreement between the Debtor and Local 55 of the Union, effective August 1, 2000 (which expires July 31, 2002).

rather, Shook seeks authority to continue to pay amounts that are due to or on account of the work of its Union Employees for the period prior to the Petition Date and which, absent this Court's authority, could not be paid during the pendency of this Chapter 11 Case.

18. Shook's Union Employees are paid each Wednesday for work performed during the week ending the previous Sunday. Union employees are paid by checks drawn on Shook's Decatur Account (described above). As of the Petition Date, there were checks outstanding to Union Employees, who had provided services to Shook pre-petition. Moreover, because the Petition Date was on April 8, 2002, Union Employees have worked from April 1, 2002 to the Petition Date, but have not yet been issued a paycheck for those pre-petition services.

19. In accordance with and as required by the Union Agreements, Shook makes contributions for health insurance, apprentice programs and welfare programs on behalf of its Union Employees (collectively, the "Union Employee Benefits," and collectively with the Non-Union Employee Benefits, the "Employee Benefits").

Relief Requested

20. By this motion, the Debtor seeks an order from the Court authorizing the Debtor (i) to pay wages due to each employee for services performed prior to the Petition Date but for which the employees had not received payment (including authority to honor checks issued pre-petition on the Decatur Account but which have not yet cleared), (ii) to pay over to the appropriate recipient all amounts withheld from employee compensation or otherwise to be contributed by the Debtor with respect to Employee Benefits and attributable to the pre-petition period, and (iii) to honor all Employee Benefits, including paid time-off earned during or attributable to the pre-petition period.

21. The Debtor estimates that gross wages due but unpaid (or for which checks were issued but had not cleared) total approximately as follows (collectively, "Pre-petition Wages"):

Salaried Employees: \$26,000;

Hourly Employees: \$10,000;

Union Employees: \$196,000.

The Debtor seeks authority to pay these amounts in the ordinary course of its business, to make all authorized deductions therefrom, and to pay to its employees the net amount of compensation due for the pre-petition period. In addition, the Debtor seeks authority to turn over all amounts withheld, whether as taxes, insurance premiums, 401(k) plan contributions or other authorized withholdings, including withholdings related to Union Employee Benefits, to the appropriate recipient in the ordinary course of business.

22. The Debtor withholds the amounts described as Employee Benefits as appropriate from employees' periodic paychecks, but in the ordinary course does not immediately turn over such deductions; rather, such deductions are remitted generally once a month. As of the Petition Date, the Debtor estimates that it has collected from employees but not yet turned over to the designated recipient, consistent with its ordinary business practice, approximately \$70,000. By this Motion, the Debtor seeks authority to pay over all such funds, including funds applicable to, or collected or earned during, the pre-petition period.

23. In addition to amounts withheld, as described above, the Debtor pays certain Employee Benefits from its own funds. For example, as is typical, the Debtor "pays" for paid time off, by permitting employees to accrue such leave to be used at later times. The Debtor also pays to its applicable insurance carriers the premiums for medical and dental insurance coverage for its employees. By this Motion, the Debtor seeks authority to continue to honor (and permit employees to use) paid time off accrued pre-petition, and to continue to make payments for the Employee Benefits for which it pays, even if such benefits were earned during or are applicable to the pre-petition period.

GROUND FOR RELIEF

24. Section 105(a) of the Bankruptcy Code and applicable case law grants the Bankruptcy Court authority to enter an order authorizing the Debtor to pay pre-petition wages and benefits. 11 U.S.C. § 105(a). Under the “necessity payment” rule (or “doctrine of necessity”), courts recognize that section 105(a) authorizes the payment of certain pre-petition obligations of a debtor when the payments are necessary to preserve the business of the debtor and to enable the debtor to reorganize successfully. See In re Braniff, Inc., 218 B.R. 628, 633 (Bankr. M.D. Fla. 1998) (court permitted the post-petition payment of certain pre-petition wage and wage-related claims as “necessity” payments); see also In re Ionosphere Clubs, Inc., 98 B.R. 174, 175-76 (Bankr. S.D.N.Y. 1989).

25. The necessity of payment rule originated in railway reorganization cases (i.e., outside of Chapter 11) where critical vendors would not supply services or materials essential to the conduct of the business until their pre-petition claims were paid. See In re Penn Central Transportation Co., 467 F.2d 100, 102 n.1 (3d Cir. 1972); In re Lehigh & New England Railway Co., 657 F.2d 570, 581 (3d Cir. 1981). The necessity of payments rule applies in Chapter 11 cases as well. See Braniff, 218 B.R. at 633 (“[a]s is often the case in operating Chapter 11 cases” the court allowed necessity payments to be made.

26. The rationale for the necessity of payment rule is that payments are in the interest of all parties, the debtors, their estates, and creditors, because the payments permit the continued operation of the debtors’ businesses. See Lehigh and New England Railway Company, 657 F.2d at 570, 581 (“[I]t is evident that the payment made under the ‘necessity of payment’ rule is in the interest of all parties, including the mortgagees, because such payment will facilitate the continued operation of the railroad.”); see also Ionosphere Clubs, 98 B.R. at 177 (determining that in Chapter 11 case the purpose of the necessity of payment rule is to prevent a debtor from going into liquidation which would result in a loss of jobs and possible misuse of economic resources). As the court in Braniff stated:

First, it was necessary that Braniff pay its employees for work performed pre-petition if the employees were to remain on the job post-petition. The filing of a bankruptcy case presents many uncertainties for employees. If their pay is interrupted, employees are obviously not going to remain on the job despite the fact that their continuation in place is vitally important for the debtor. Second, in any event, the pre-petition wages are subject to the priority of section 507(a)(3). Thus, in all but the direst of circumstances, the debtor will ultimately pay the pre-petition wages because of their very high priority.

218 B.R. at 633.

27. Courts commonly apply the necessity of payment rule to permit the payment of pre-petition claims by employees, recognizing that the services of skilled employees are essential to the continued operation and reorganization of the debtor. *Id.*; *In re Gulf Air, Inc.*, 112 B.R. 152, 153-54 (Bankr. W.D. La. 1989) (payment of pre-petition wages, business expenses, health and life insurance premiums, and worker's compensation premiums were "indispensable" to successful reorganization of debtor); *Ionosphere Clubs*, 98 B.R. at 177 (referring to the court's authorization of payment of pre-petition wage, salary, medical benefit, and business expense claims of active employees). The necessity of payment rule clearly extends not only to wages, but also to business expenses, health and life insurance premiums, and workers' compensation premiums. *See Gulf Air*, 112 B.R. at 153.

28. Authority to pay pre-petition wages and benefits is essential to the Debtor's continued business operations and efforts to reorganize. As a service-oriented business, Shook depends upon the skill, expertise and commitment of its employees to continue in business; it cannot operate its business without the labor and skill of its employees. Loss of key employees, or indeed of any significant number of employees, would impose great burdens and risks upon the Debtor's business and its prospects.

29. If the Debtor is allowed to pay the pre-petition wages and benefits, the Debtor likely will be able to retain its employees and continue to operate its businesses, and thus continue with its efforts to reorganize. Without the authority to pay wages and benefits to its employees, many of whom depend upon regular receipt of their wages and benefits for their

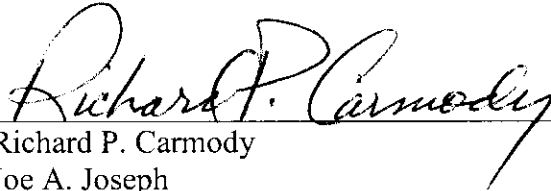
overall well-being, Shook faces the loss of employees and the resulting damage to its business. The loss of a material number of employees would leave the Debtor unable to continue operations of its business. The Debtor may be forced to liquidate, with an attending loss of jobs for the remaining employees and loss in value of the Debtor as a going concern. Accordingly, in the business judgment of the Debtor, payment of the Pre-petition Wages and Employee Benefits is necessary for the Debtor to continue its business operations and efforts to reorganize and therefore, is in the best interest of the Debtor, its estate, the employees, and creditors.

30. Moreover, the claims of employees for wages and benefits earned in the 90 days preceding the Petition Date (and within 180 days for employee benefit plan payments) would be allowed as priority claims under §§ 507(a)(3) and (4) of the Bankruptcy Code, up to the \$4,650 per employee limitation set forth therein. Because the Plan provides that all such priority claims will be paid in full, the Debtor submits that payments of such claims at this time will not affect any other creditor or party-in-interest, and is in the best interest of the Debtor's estate and its creditors.

31. While the Debtor believes that no employee will receive pre-petition wages or benefits in excess of the priority claim limits set forth in § 507(a)(3) and (4), out of an abundance of caution, and to avoid any later dispute, the Debtor seeks authority also to make payments to employees in full, in the ordinary course of business, even if such payments would exceed the priority claims amounts. While amounts above that limit would generally be viewed as unsecured pre-petition claims, such operational claims are also to be paid in full under the Plan. Accordingly, the Debtor submits that payments of such claims, if any, at this time will not affect any other creditor or party-in-interest, and is in the best interest of the Debtor's estate and its creditors.

WHEREFORE, for all these reasons, the Debtor respectfully prays that this Court enter its Order authorizing the Debtor to the pay the Pre-petition Wages and Employee Benefits to the Debtor's employees as set forth herein, and granting such other and further relief as the Court deems proper.

Respectfully submitted,

A handwritten signature in cursive script, reading "Richard P. Carmody", is written over a horizontal line.

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Dated: April 8, 2002

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
Southern Division**

In re:

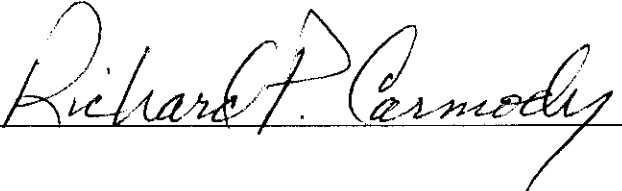
SHOOK & FLETCHER INSULATION CO.

Debtor-in-Possession.

**Case No. _____
Chapter 11**

CERTIFICATE OF SERVICE

I hereby certify that on this 8th day of April, 2002, I caused a copy of the foregoing Motion for Authority to Pay Pre-petition Wages and Benefits to Employees and proposed Order to be served upon the parties on the attached Service List in the manner indicated.



**Shook & Fletcher Insulation Co.
Attachment to Certificate of Service**

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* Parties designated with an asterisk were served by hand-delivery. All other parties were served by overnight mail.